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SUBJECT: CAN PERU IMPROVE COMPETITION IN TELECOMS INDUSTRY?

Ref: Lima 984

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11. (SBU) Summary. Two recent developments in the telecommunications industry have GOP officials pointing to improved competition in the market. America Movil, a Mexican company owned by Carlos Slim, acquired the fourth mobile band on March 30 and should begin operations by early 12006. The Ministry of Transportation and Communications (MTC) formally approved the merger of Telefonica del Peru and BellSouth on April 8. MTC, in return, demanded that Telefonica give up one of its two frequency bands (as part of the MTC spectrum clean up) and commit to expand mobile service to 2,000 communities. Despite GOP efforts to open the market to new mobile participants, competition in the telecommunications market is still limited, as Peru's excessive mobile termination rates benefit Telefonica vis-a-vis other providers. End Summary.

Limited Competition But Room For Growth

12. (U) Although Peru is experiencing unprecedented economic growth, this is not mirrored in the mobile telecommunications sector. In 2004, there were only four million users, a significant increase from 2.9 million users in 2003. Telefonica del Peru, with 67.5 percent of the market, dominates Peru's mobile market. Italy's TIM Mobile ranks second, with 26.9 percent, and Nextel is third with 4.5 percent. Of note for future competition: China's Huawei recently successfully completed a pilot of low-cost mobile phones in the 450-mgH band in Peru.

America Movil Wins Fourth Band

13. (SBU) America Movil, a Mexican company owned by millionaire Carlos Slim, was awarded Peru's fourth band on March 30. According to the MTC, America Movil only paid \$21.1 million for the spectrum, considerably more than the \$180 million TIM paid to enter the market in 2002. America Movil, using GSM/GRPS technology (which is compatible with the TIM system), will begin operations in Peru by late 2005/early 2006. According to Carlos Slim, Sercotel's (as the Peruvian company will be known) entry into the market will help drive down Peru's high mobile costs.

14. (SBU) America Movil was the sole bidder on Peru's fourth band, even though Nextel was expected to submit an offer. Alfonso de Orbegoso (protect), Vice President of Legal Affairs at Nextel Peru, informed Commercial Counselor in mid-March that a Sprint (Nextel's parent company) assessment of the project determined that the high termination rates (averaging \$0.21) and the unwillingness of Osiptel to act quickly were limiting factors in Nextel's ability to compete in the market. As a result of these factors, Nextel's Peru based finances were deteriorating, making it financially unable to bid on the fourth band. Furthermore, unless Osiptel regulates the high mobile rates soon, Nextel will face serious financial difficulties in Peru, limiting the company's ability to expand service throughout the country.

BellSouth Merger Approved

15. (U) After months of deliberation, the MTC formally approved the merger of Telefonica del Peru and BellSouth on April 8. MTC's approval, however, came with a multitude of draconian stipulations. First, Telefonica must give up one of its two frequency bands within the next two years, which the MTC will open to bidders by the end of 2007. (Note: This is part of the MTC's plan to clean up spectrum, which will affect all mobile providers. End Note.) Additionally, Telefonica must waive the fees for former BellSouth clients who wish to cancel service. (Under Peruvian law, customers must pay the entire cost of the service contract if the contract is cancelled early.) Third, Telefonica must expand or improve mobile access to a minimum of 2,000 communities

in the poorest areas of Peru by 2008. Failure to do so will result in a fine of 16,500 soles (\$5,077) per community, paid to MTC. Fourth, Telefonica is prohibited from including former BellSouth customers on its on-net plan until 2007. Finally, the MTC noted that if OSIPTEL finds Telefonica guilty of committing five infractions (cross subsidy, predatory pricing) in a two-year period, Telefonica would lose its concession. Furthermore, if Telefonica commits two infractions in one year, it will also lose its concession of BellSouth.

Comment: Increased Competition?

16. (SBU) Peru's telecommunications industry, particularly the mobile sector, is underdeveloped. There is a huge potential for growth and the entrance of America Movil, as well as the merger of Telefonica and BellSouth, should marginally improve competition between mobile providers. However, the GOP must grapple with Peru's high mobile termination rates, which continue to undermine competition in the market. Telefonica, which controls over two-thirds of the market, allegedly continues to use predatory pricing and cross subsidies to keep its on-net rates low. These practices should cease when the new mobile rate takes affect in June. If not, Nextel now has a means by which to bring its complaints to MTC, which ultimately may cause Telefonica to lose its concession of BellSouth.

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